

**Testimony on behalf of  
Commercial Real Estate Interests in Michigan  
Senate Economic Development Committee**

**February 29, 2012**

Good morning Mr. Chairman and committee members. I am Michael Berger of Berger Realty testifying on behalf of commercial real estate owners, investors, and developers in Michigan regarding Senate Bill 992. With me is Janet Langlois, Executive Director for Building Owners Managers Association of Southeast Michigan. Thank you for the opportunity to address you regarding this important issue.

Commercial mortgage loans provide the capital for development of commercial properties that are the buildings we live and work, shop and play in. They are a significant contributor to the U.S. economy — generating or supporting some 9 million jobs, roughly one-quarter of GDP, and over two thirds of local government tax revenue. These developments provide immediate relief in an economic downturn by creating construction jobs and asset value contributing to the municipal tax base. Further, commercial real estate development, construction and operations create a ripple effect in the economy. After new buildings are completed and occupied, they add to the productive capacity of their host economies. Buildings require a continuing flow of expenditures to support their operations, including management, maintenance and repair, cleaning and custodial services and utilities. It is estimated that every \$1 spent generates an additional \$3.42 that we otherwise would not see flowing through our economy.

Some of these commercial loans are made by banks and other lenders as **Nonrecourse Mortgage Loans** and then pooled and sold by Wall Street companies as investments known as commercial mortgage backed securities (CMBS.) The lender's risk and reward for making a loan is assessed through underwriting including an analysis of the revenue from tenant rents in relationship to the expenses of operating the property and the repayment of the loan. Through this assessment, the lender evaluates the adequacy of the cash flow to pay principal and interest on the proposed loan as well as operating expenses and the risk of a default by the borrower. **Nonrecourse carveouts** are limited exceptions to the nonrecourse nature of the mortgages securing CMBS loans (such as the borrower taking the rents that belong to the lender after a default.) The lender takes the risk of a decline in the property's ability to collect rent and other inherent risks such as economic factors that could drive property values down. In the event of a default, the lender's remedies are limited to taking the property and the rents and the borrower is not liable for anything other than giving the lender the property.

A **Nonrecourse Mortgage Loan** allows the borrower to limit its financial exposure on a project to the equity it invests in the project and does not put the developer's other assets at risk through the use of a Single Purpose Entity (SPE), an ownership entity. **This type of loan vehicle is an important tool in attracting investment grade development to Michigan.** It is extremely important in times of economic downturns where property values may be significantly depressed. If borrowers are required to put their personal assets at risk, *many existing projects would never have gotten off the ground.*

In Michigan last year, despite a very sluggish economy, CMBS loans in Michigan totaled \$93.9 Million dollars. All told, there are over \$13.8 billion of CMBS Loans on Michigan properties; many of which have

lost significant value in the Great Recession and whose owners could be facing personal liability never intended by either party (the lender or the borrower). If any of these developments were to become insolvent, and Wall Street firms were allowed to cash in on the personal assets of the borrower, it very well may put many of them out of business and in bankruptcy, further crippling Michigan's economic recovery.

There is no other state that holds a nonrecourse guarantor liable simply because a borrower becomes insolvent. It simply was never contemplated by the parties who made the nonrecourse loans. This was specifically addressed in a recent court case where the originator and architect of the loan documents, Goldman Sachs, testified that the borrower's insolvency was the lender's risk and did not constitute a SPE violation and that the plaintiff's argument was contrary to the central premise of a CMBS loan.

**We must ensure that a Nonrecourse loan remains a Nonrecourse loan as was originally intended by the parties. The proposed legislation, SB 992 will strengthen Michigan's goal as a competitive business investment environment encouraging development which will support our state economy and ensure our future prosperity.**

Respectfully Submitted,

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